



## ANALYSIS OF THE IMPLEMENTATION AND IMPLICATIONS OF OECD/G20 PILLAR ONE ON THE TAXATION SYSTEM IN INDONESIA

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### Abstract

*One of the efforts taken by member countries of OECD/G20 Inclusive Framework for BEPS is to capture tax revenue from the digital economy is called Pillar One: Unified Approach specifically Amount A. This research aims to obtain information on the progress and obstacles on the implementation of Pillar One in Indonesia, including the impact generated by Pillar One as well as understand policy alternatives that could potentially become replacement for Pillar One. The method used in this research is qualitative with a case study approach. The results obtained in this study show that currently Pillar One cannot be implemented because it encounters various obstacles and is related to other jurisdictions. If Pillar One has been implemented, the implications are additional tax revenue potential but relatively low, adjustment on policy, tax administration systems, IT systems and human resources. Pillar One, which has the potential to be canceled, raises alternative policies that can be implemented by Indonesia such as Digital service tax, Article 12B UN Model Convention and new PE criteria namely Significant Economic Presence. The government must reconsider the cost and benefit on implementation of Pillar One. The government must also prepare and compile alternative policies and supporting aspects such as IT system development due to the potential failure of the Pillar One implementation.*

**Keywords:** Digital Service Tax, OECD/G20, Pillar One, Tax Avoidance

### INTRODUCTION

The development of technology, information, and communication has had a significant impact on various aspects of human life, including taxation. Fluctuating trends in tax revenue realization can also be attributed to factors such as the advancing technology. According to the World Bank (2021) and based on United Nations Conference on Trade and Development (UNCTAD), technological advancement began in 1990 and rapidly increased from 2015 to 2020. UNCTAD (2021) also states that the use of digital data via the internet is increasing, with varying numbers in each region. Technology also forces all aspect to changes, including changes in transaction business model, which now more often happening digitally, known as e-commerce. Those fact also supported by data from UNCTAD (2021), which shown 80% of internet users in Europe use e-commerce.

The digitalization challenges arise due to the influence of Multinational Enterprises (MNEs) which exploiting one of digitalization impact named digital economy. Digitalization greatly benefits MNEs in terms of business processes, such as sales redirection and transitioning from country-specific models to global models (OECD, 2013). Another challenge which arises from digitalization of MNEs is the use of intangible assets. OECD (2013) states that digital based business tends to have more intangible assets. This is undeniable because intangible assets are crucial factors from company's production (Hall, 2001 as cited in Dischinger & Riedel, 2011). Intangible assets also pose challenges because they are more difficult to measure in value and easier to transfer or relocate by the company (Li, 2018; Beer & Loeprick, 2015 in Dabla-Norris et al., 2021; Worokinasih et al., 2022). Most MNEs also can transfer intangible assets to countries with lower tax rate (Dischinger & Riedel, 2011).

Aside from intangible assets, digitalization allows MNEs to established their business without physical presence. This is possible due to the emergence of various new business models such as e-commerce, cloud computing, digital content subscription, application stores, online payment services, and so on (OECD, 2015). With these new business model, MNEs can



operate remotely or without physical presence (Szczepanskik, 2020). It can be concluded that digitalization removes the concept of physical presence or Permanent Establishment (PE) (Hongler and Pistone 2015; Martin Jimenez, 2018 in Ponomareva, 2019). MNEs can get a benefit in taxation when the concept of physical presence is removed. It is because according to (OECD, 2015), most of domestic tax laws and tax treaty still require physical presence for imposing taxes on an MNEs. The benefit which MNEs get is in the form of profit shifting which leading too double non-taxation (Worokinasih et al., 2022). Therefore, it can be concluded that digitalization enables MNEs to reduce their tax burden by shifting tax liabilities from countries with high tax rates to those with lower tax rates (OECD, 2013).

Profit shifting issues, particularly due to digitalization, have become a global discussion known as Base Erosion Profit Shifting (BEPS) (OECD, 2013). There are many examples of large companies engaging in profit shifting practices. Reuters (2013) reported that companies like Apple, Google, and Amazon have been involved in profit shifting. An examination of Apple Inc. revealed that during the period 2011-2013, it only paid 2% of its total income, which reached \$74 billion. The fact shows that Apple engaged in tax planning by shifting profits to Ireland.

Based on the events and the significant potential of BEPS, the Organization for Economic Co-operation and Development (OECD) and the G20 countries formed a discussion group called the OECD/G20 Inclusive Framework on BEPS. In 2013, the OECD/G20 Inclusive Framework on BEPS agreed upon 15 action plans related to BEPS, commonly known as the Base Erosion Profit Shifting Action Plan. Among these action plans is addressing the challenges of profit shifting caused by the digital economy (OECD, 2013).

OECD/G20 inclusive framework on BEPS states that a consensus-based approach must be made to comprehensively address the issues of digital taxation rights and reduce the potential for MNEs to engage in profit shifting (OECD, 2019). OECD/G20 Inclusive Framework on BEPS proposed a solution called the Two-Pillar Solution as one of the solutions to tackle BEPS in the aspect of the digital economy. There are two main pillars proposed as a comprehensive solution, namely Pillar One (Profit Allocation using Unified Approach) and Pillar Two (Global Anti Base Erosion (GloBE) Rules). Specifically, Pillar One includes three provisions: Amount A, Amount B, and Tax Certainty. Amount A can be understood as a method of profit allocation aimed at allocating taxation rights over MNE profits to the countries where the income is generated, while Amount B involves simplification of the Arm's Length Principle and accommodation in case of disputes in the application of Amount A (Tax Certainty) (OECD, 2013). As of 2021, 137 countries and jurisdictions have joined the plan for implementing these two pillars as a solution to address profit shifting in digital economy. The Two Pillar Solution was planned to be implemented in 2023 but it was postponed until 2024 (Arief, 2022).

Harpaz (2019) states that one of the reasons why Pillar One was postponed is because the MNEs targeted by Pillar One mainly reside in high-economic jurisdictions, such as the United States. The United States, as one of the high-income jurisdictions would lose revenue as a result of the implementation of Pillar One (Eden, 2021a as cited in Eden, 2021c). With the existence of Pillar One, MNEs which headquartered in the United States, would distribute profit globally to the jurisdictions of MNEs' market and potentially reducing the tax income collected from the MNEs in the United States. Navarro (2021) stated that the rejection of agreement on Pillar One is based on five aspects, including: 1) Under the current international tax regime, countries like the United States benefit greatly; 2) The scope of Amount A is not limited solely to digital MNEs but also to MNEs that meet a specified threshold; 4) Pillar One would eliminate unilateral measures such as digital taxation already implemented in the United States; 5) Pillar One requires significant support for dispute resolution mechanisms.



Although there is potential of failure, according to Surono & Apriliasari (2022), Pillar One could accommodated the interest from market jurisdiction of the MNEs which usually belong to the group of developing countries. The aim of Pillar One is to distribute fair taxation rights among market countries over the profits received from there to MNEs (OECD, 2022). This relates to one of the provisions set out in Pillar One, namely Amount A, which entails a fairer profit allocating by allocating residual MNEs' profit (OECD, 2021).

Various studies have been conducted to examine the tax potential Amount A and its impact to the tax administration. Some studies indicate that the implementation of Pillar One Amount A will have a positive impact on developing countries that become as a market jurisdiction for MNEs, such as Indonesia. One of these positive impacts is the increase in tax revenue in market jurisdiction from the income received by digital MNEs. This is mentioned by Li (2018) and Tambunan (2021) in their research, highlighting the potential increase in tax revenue that developing countries could experience due to the implementation of these provisions. The potential increase in tax revenue for market jurisdiction, which are middle-income countries like Indonesia, is estimated to be around 5 percent or 0.02 of GDP (Dabla-Norris et al., 2021).

However, there are other studies which shown the contrary result. Dabla-Norris et al. (2021) and Jacobs (2022) states that on the contrary, developing country including Indonesia are not expected to benefit significantly from the implementation of the provisions in Pillar One. Dabla-Norris et al. (2021) states that the potential revenue gain for these developing countries is very low or even the opposite, with the possibility of them to losing revenue around 0.01 percent of GDP. Bauer (2020) also mentions a similar concern that the provisions in Pillar One could potentially shift taxing power from developing countries to developed ones.

It is also stated that Amount A in Pillar One could result in tax complexity or a complicated tax system and also create uncertainty. Similar research has been conducted to see the impact in tax administration. Parada (2019) states that Pillar One may not necessarily be effective because of the enforceability against MNEs is still in doubt. Pillar One is also considered to potentially increase complexity in its implementation, particularly regarding Amount A (Navarro, 2021 as cited in Surono & Apriliasari, 2022). The implementation of Pillar One also requires readiness from tax authorities, both in terms of human resources and IT systems (Tambunan (2021) and Worokinasih et al. (2022)).

Based on these factors, Pillar One may generate potential tax revenue from allocations in accordance with Amount A, but also has the potential to bring about various challenges and obstacles if implemented in Indonesia. Therefore, this research aims to obtain information and understand the implementation plan, including the challenges that arise in the plan. Additionally, it will also examine the impacts or implications of implementing Pillar One on the tax system in Indonesia, including administrative aspects, resources, and potential tax revenue. In discussing the implementation and implications of Pillar One in Indonesia, the author will also relate to the provisions set out in Pillar One, especially those covered in Amount A, which are related to new taxing rights for countries where multinational enterprises (MNEs) conduct their business or provide services.

## **LITERATURE REVIEW**

### **Theory of Planned Behavior**

The Theory of Planned Behavior is one of the theories that can be used to describe tax compliance. Ajzen (1991) as cited in Benk et al. (2011) stated that the Theory of Planned Behavior can be interpreted as behavior that is or is not performed by an individual based on their intention and belief regarding the behavior to be performed. Kunarti (2019) argues that this theory is related to the total control actually possessed by an individual. The control



possessed by individuals in terms of achieving certain goals tends to be directed towards realistic aspects and possibilities that may occur in the process of achieving the goals. When associated with the concept of taxation, control can be caused by the positive and negative impacts of taxation displayed in the media (Kunarti, 2019). There are three types of behavior in this theory according to Ajzen (1991) as cited in Hasanah & Ardini (2021), namely Behavioral Belief, Normative Belief, and Control Belief.

### **Compliance Tax Theory**

Tax compliance stems from the concept of compliance. Compliance can be understood as an action that aligns with the law, while non-compliance can be interpreted as actions that conflict with the law (Richardson & Sawyer, 2001). Roth and Witte (1985) as cited in Hasiholan and Jasman (2019) state that tax compliance is acting in accordance with tax obligations that are the responsibility of taxpayers, such as timely tax administration reporting with the correct amount of tax due based on applicable regulations. Richardson and Sawyer (2001) add that tax compliance can be defined as the willingness or readiness of taxpayers to act in accordance with tax regulations and their awareness to pay the tax due. On the other hand, Tilahun (2019) also concludes that tax compliance is the action of taxpayers in accordance with applicable tax regulations.

### **International Taxation**

International tax law is never specifically defined. According to Arnold (2019), international taxation is defined as the international aspect of each country's domestic tax law, including the taxation of domestic taxpayers on income earned abroad, and the taxation of foreign taxpayers on income earned domestically, which constitutes domestic tax law that serves as provisions for international taxation. International taxation is closely related to Tax Treaties, which according to Pohan (2018), are tax agreements between two countries (bilateral) made with the aim of minimizing double taxation and various tax avoidance efforts.

Currently, international taxation faces challenges with the existence of the digital economy, which according to OECD (2013), involves the extensive use of data, utilization of intangible assets, and when associated with business processes, digitalization will make it difficult to determine the jurisdiction where products or value are produced. Many countries feel the need for reform in international taxation because of the increasing cross-border transactions and countries that cannot levy income tax on parties benefiting from these transactions (Mason, 2020). Therefore, there is a need for fundamental changes in international taxation that focus on current conditions, such as profit shifting, or as termed by OECD, Base Erosion Profit Shifting (BEPS) (Clavey et al., 2019).

### **Tax Avoidance**

Taxpayers' efforts to minimize the amount of tax due constitute resistance, with tax avoidance being the act of minimizing tax liabilities, as noted by Pohan (2018). This resistance encompasses both direct and indirect means to avoid taxes, potentially reducing state revenues, as outlined by Satyadini (2018). There are many factors that influence tax avoidance and tax evasion. Transparency, complexity, and tax injustice affect the desire to engage in tax avoidance (Bako, 2021). Different opinions are presented by Salsabila & Diantimala (2023), stating that investments, performance, and financial conditions affect the increase in tax avoidance in a company. Another factor mentioned by Ramadhan (2023) is thin capitalization, where the amount of debt exceeds the capital. Thin capitalization can increase tax avoidance due to high interest expenses, so when the thin capitalization rule is applied, the level of tax avoidance can decrease.

Another form of tax avoidance practice can be transfer pricing, and according to Irawan & Ulinnuha (2022), transfer pricing is defined as a form of tax avoidance by shifting profits from countries with high tax rates to those with low tax rates. The existence of transactions



between related parties also increases the potential for transfer pricing (Rezeki et al., 2021). This opinion is also supported by Irawan & Ulinuha (2022), who state that the more "multinational" or the more a company operates in various countries, the higher the transfer pricing or transfer pricing aggressiveness will be. Multinational companies based on intangible asset ownership will also increase the aggressiveness of transfer pricing (Yunidar & Firmansyah, 2020).

### **Internalization Theory**

The internalization theory is related to the term OLI Paradigm (Hennart, 2009 as cited in Darussalam et al., 2013). This is because MNEs are also based on the OLI paradigm, as stated by Dunning and Lundan (2010). The connection between internalization theory and the OLI paradigm is that the OLI paradigm represents the benefits of implementing internalization theory, which according to Darussalam et al. (2013) consists of Ownership Advantages, which depict the reasons multinational companies can enter international markets; Location Advantages (L), which form the basis for placing multinational companies in their operations; and Internalization Advantages (I), which are related to how multinational companies enter international markets.

### **METHODS**

This research aims to obtain information and understand the planned implementation, including the constraints that arise in the plan. Additionally, it will also examine the impacts or implications of implementing Pillar One on the taxation system in Indonesia, including administrative aspects, resources, and potential tax revenue. The analysis will be based on data from opinions and facts according to relevant parties. Therefore, the author uses a qualitative approach. The goal is to gain in-depth understanding of the existing issues to obtain results that align with the research objectives. This is in line with what was stated by Sugiyono (2012) where qualitative research is more based on background, utilizes humans as research tools, employs inductive analysis, and focuses on the research process rather than the research results.

Qualitative research can be conducted using various methods, as stated by Sekaran and Bougie (2016), including experiments, survey research, observation, ethnography, grounded theory, action research, and mixed methods. OECD Pillar One is a current issue and phenomenon in international taxation. Understanding must be based on this phenomenon, so in this study, the method used by the author is a case study method. A case study can be defined as a scientific research activity that is intensive, in-depth, and detailed about programs, events, and activities at various levels, from individual to organizational levels, with the aim of obtaining information about the case (Rahardjo, 2020). Yin (2008) states that the essence of case study research is to explain the reasons behind the selection of the study, how to implement it, and what the results are.

Based on the research objectives outlined earlier, which are to analyze all aspects related to the implementation plan of Pillar One in Indonesia, the type of data to be used is primary data sourced through interviews with competent sources in the field of international taxation, especially those knowledgeable about the OECD/G20 BEPS Action Plan, specifically Pillar One Amount A with the details as follows:

- a. Informant one (I1) is one of the employees at the Fiscal Policy Agency who is regularly involved in discussions on Pillar One
- b. Informant two (I2) is an employee who is a member of the special team for the Country by Country Report (CbCR) at the Directorate of International Taxation, Directorate General of Taxes.





- c. Informant three (I3) is an employee who is a member of the special team for the digital economy (Task Force for Digital Economic) at the Directorate of International Taxation, Directorate General of Taxes.
- d. Informant four (I4) is an employee of the Directorate General of Taxes who is an expert in international tax.
- e. Informant five (I5) is a tax consultant with expertise in international taxation.
- f. Informant six (I6) is an International Tax Lawyer who understands Pillar One.

The number of informants is not binding and not limited. It can decrease or increase because in qualitative research, there is no predetermined minimum or maximum number of informants or sources (Heryana, 2018).

In conducting the research, the researcher will use the triangulation method. According to Sekaran and Bougie (2016), triangulation method is one way to combine several sources used in qualitative research. Moleong (2006) as cited in Wandu (2013) states that triangulation is one way to examine data by utilizing other factors outside the data itself. Sekaran and Bougie (2016) add that triangulation is not only in terms of method usage but can also involve data, theory, and even the researcher. Some methods that will be used by the researcher include documentation, interviews, and literature review.

The method used in this qualitative data analysis is the Miles and Huberman Model. According to Sekaran and Bougie (2016), data analysis using the Miles and Huberman model involves three main components:

- a. **Data Reduction**  
Data reduction, is related to the process of selection, coding, and categorization of data. Coding is a stage for analyzing qualitative data by reducing, sorting, and integrating it into a theory. The purpose of coding is to assist researchers in drawing conclusions. Data categorization is the process of organizing, arranging, and classifying the results of coding into codes.
- b. **Data Display**  
According to Miles and Huberman (1994) as cited in Sekaran and Bougie (2016), Data Display is the second stage in qualitative data analysis. Data Display can be understood as the process of presenting the reduced data in an organized form. Data Display can be aided by using graphs to facilitate data organization, thus forming patterns and relationships that lead to drawing conclusions.
- c. **Drawing Conclusion**  
This stage is the final stage of the qualitative data analysis process. In this stage, researchers answer the research questions by explaining the patterns and relationships found, making comparisons, and determining the significance of the identified themes.

## **RESULTS AND DISCUSSION**

### **Pillar One Implementation**

Optimism and skepticism are seen the implementation plan of Pillar One in Indonesia from the perspective of the government, namely the Directorate General of Taxes and the Fiscal Policy Agency. This was stated by all informants who expressed doubts that Pillar One could be implemented in Indonesia. This fact is also unfounded because considering the dynamics that occur, especially from a global perspective, Pillar One may also be difficult to implement. This potential is indicated by the process of discussing Pillar One, as shown by the stages of signing the Multilateral Convention (MLC), which has been pushed back since the issuance of the outcome statement by the OECD/G20 Inclusive Framework on BEPS (IF) in October 2021 until the latest outcome statement in July 2023.



The Outcome Statement is a statement issued by the OECD/G20 regarding the outcomes of the discussions on the Two-Pillar Solution implementation plan and contains the agendas that have been and will be carried out in the future. In the October 2021 Outcome Statement (October Statement) contains important points regarding MLC. The MLC, which regulates the provisions of Pillar One, is used as a multilateral framework tool by countries that surpass the double tax agreements (DTAs) or tax treaties. Tax treaties will still apply, but the MLC will accommodate if there are provisions in the Tax Treaty that may potentially lead to disputes regarding Pillar One Amount A.

The October Statement contains points stating that the signing of the MLC was opened in 2022 with the hope that Pillar One, specifically Amount A, would be implemented in 2023. According to Informant one, the member of IF may indeed sign the MLC, but for the MLC to be implemented and binding, it requires ratification. Provisions in the MLC that becomes concern to each member country include the elimination of all forms of digital taxation or similar measures when Pillar One is established. Additionally, all member countries are not allowed to impose digital taxes during the period from October 8, 2021, until the beginning of December 31, 2023. Both points, signing and ratification, as well as the elimination of digital taxes, pose obstacles to the global adoption of Pillar One Amount A, as outlined in the July 2023 Outcome Statement.

Indications of problems arise in the global implementation efforts of Pillar One are evident from the July Statement. Generally, the July Statement contains concepts that have been outlined in previous statements, along with changes resulting from dynamics among jurisdictions. This is reflected in the point stating that there are several jurisdictions (countries) that have concerns about the content of the Pillar One MLC. The impact of this point shown by the delay in the signing of the MLC, which was opened in the second half of 2023. Pillar One is planned to be implemented in 2025. It is not unlikely that there will be a setback in the implementation timeline. Regarding the signing of the MLC, if the critical mass has not been reached, as indicated by not fully 30 countries representing 60% of the Ultimate Parent Entities (UPEs) agreeing, Pillar One will be hard to implemented.

According to data from Forbes (2023) on 2000 multinational enterprises (MNEs), it is revealed that among the top 100 companies, 38 are located in the United States. Furthermore, looking at the overall data, there are 611 companies originating from the United States, totaling 1/3 of the top 2000 companies. Referring to the data presented by Starkov and Jin (2022), in 2020, the United States had 37 MNEs with profit before tax (PBT) exceeding the Pillar One threshold of EUR 20 billion. This number would increase to 70 MNEs in line with the OECD (2021), which indicated that the threshold could be lowered to EUR 10 billion in the future. This data serves as one of the reasons why the United States tends to show disagreement with the provisions of Pillar One. Informant one conveyed that the main challenge faced currently is the resistance efforts undertaken by the United States. According to him, this resistance has been formally declared by the United States Congress. Both informant one and informant three also added that this resistance has reached the point of threatening not to contribute mandatory dues to the OECD, where the United States accounts for 20% of the OECD's annual funding.

The actions taken by the United States further indicate that it will not sign the MLC, which is intended as a commitment to implementing the provisions of Pillar One. The main reason for this disagreement is once again related to the concept of Pillar One Amount A, which can be simplified as the concept of dividing the pie. Here, the "pie" represents the taxation rights over the profits of MNEs received by the country with a large economy where the headquarters or UPE is located. This "pie" is then distributed to the countries where the subsidiaries of the UPE generate profits.



This serves as the reason for the United States' reluctance to share or allocate its taxation rights to other countries, considering that most multinational corporations falling under the scope of Pillar One are based in the United States. The United States, represented by its Senate, feels it is unfair because the contribution of taxation rights to the largest market jurisdiction seems to come predominantly from them, posing the potential for a decrease in tax revenue in the country. This sentiment was also conveyed by informant three, who stated that even the United States Senate has sent a letter to OECD representatives regarding this matter. The actions of the United States will trigger similar actions by other countries because Pillar One intersects with the national interests of each country, especially those countries serving as the main capital location or home country of an MNE.

Pillar One is a multilateral consensus that, in its implementation, requires approval from the countries involved, in this case, the member countries of the inclusive framework. The issue faced by the United States is one of the constraints experienced in a multilateral agreement. There are interests that must be upheld by a country considering the cost and benefit of the agreement to be approved. Informant two stated that in the global-level discussions of Pillar One Amount A, countries are very attentive to what they will receive and what they will give. From the perspective of the contributors, they must consider whether they are willing to allocate a portion of their rights to the market jurisdiction countries. On the other hand, countries receiving profit allocations also consider the portion they should receive. In large market countries like Indonesia, this is a significant concern. Considering what was conveyed by Wijaya & Utamawati (2018), who stated that the digital market potential in Indonesia is enormous. Therefore, according to informant two, the discussions on Pillar One encountering obstacles and not being able to be applied globally are due to the lack of agreement among member countries, considering the balanced consideration of benefits and losses.

The same issue also poses considerations for Canada not to fully commit to the implementation plan of Pillar One Amount A as outlined in the July Statement. Regarding national interests, as of January 1, 2024, Canada will impose a Digital Service Tax (DST) at a rate of 3%. This action is not in line with what is stated in the July Statement regarding the prohibition of implementing digital taxes and similar measures by January 2024, but can be extended until December 31, 2025, or upon entry into force of the MLC Pillar One. According to informant three, Canada implements DST based on the fact that many countries have previously and are still implementing DST, considering the provision in Pillar One which is not to apply DST. This reason is considered reasonable given the potential revenue from digital transactions as stated by Eden (2021b) and the planned implementation of Pillar One, which is still scheduled for 2025 and still full of certainty.

Moscrop (2023) states that Canada will not wait for the implementation of Pillar One Amount A, even though many parties, including Canadian businesses and the United States, see the potential losses incurred in implementing unilateral actions. According to informant six, the United States can file arbitration with the World Trade Organization (WTO), which seems to be a threat to Canada that disagrees with the ban on the implementation of Pillar One. However, according to Chrystia Freeland's statement in PWC (2023) as the Deputy Prime Minister and Minister of Finance of Canada, Canada supports MLC Pillar One but does not accept any extension of time.

Looking at the issues happening in Canada, it can be seen that the implementation of Pillar One will trigger countries to adopt unilateral policies. It is undeniable that in the course of implementing Pillar One in 2025, there will be countries taking the same action, namely implementing DST, as 138 countries have agreed to extend the ban on new DST implementations. This is what will happen with the African Tax Administration Forum (ATAF), where ATAF will coordinate with African Union members to implement DST to





prevent loss of revenue from digital transactions. Informant six also adds that the longer Pillar One is implemented, the more countries will feel "fed up" and will certainly prepare digital tax service provisions.

The global issues related to Pillar One Amount A that are currently hot are reducing optimism about the implementation of Pillar One in Indonesia. Informant two believes that all possibilities can happen, including the cancellation of Pillar One implementation. Informant one and Informant three also express pessimism about the implementation of Pillar One. It all comes back to the global situation, especially the political conditions, where countries with greater economic power tend to pull other countries in different positions, causing a tug-of-war situation as currently shown by the United States. Informant three also adds that Pillar One is highly dependent on the dynamics in the United States.

Reinforcing the opinions of the informants, informant six is also very certain that Pillar One cannot be implemented globally. The potential failure of Pillar One implementation is due to the dynamics of rejection from the United States. In addition to feeling unfair about profit sharing with other countries, another reason, according to informant six, is the reluctance of the United States to use multilateral agreements above their domestic regulations. Historical data presented by Goulder (2023) shows that the United States has also refused to sign a multilateral instrument related to BEPS eight years ago.

In addition to the dynamics in the United States, Pillar One also seems to benefit OECD member countries, most of which are source countries where UPEs are located. According to ATAF (2023), Pillar One Amount A will only lead to very limited allocations in African countries. Furthermore, Pillar One Amount A does not address the emerging issue of the imbalance in profit distribution between home countries and market countries, causing losses. This is shown by the statement of Dr. Lyla Latif in a webinar with PKN STAN (2023) that African countries are not ready for the implementation of Pillar One. This condition is also indirectly related to the research by Barake & Pouhaër (2023), which states that Pillar One has the potential to benefit developed countries.

From the perspective of businesses, particularly MNEs, Pillar One is unlikely to succeed given the complexity of its provisions. This was directly conveyed by Sebastian De Buck, the tax director of a large multinational company operating in Indonesia, Unilever, during a webinar hosted by PKN STAN (2023). Sebastian De Buck stated that Unilever Group is currently in the process of observing the technical aspects of Pillar One. Despite being within the scope of Pillar One, the Unilever Group operates with a decentralized business process, with residual profits already allocated to subsidiaries in each market jurisdiction. This makes the Unilever Group skeptical about the Pillar One scheme, including the allocation of profits among countries. This skepticism was further emphasized by Wobke Hählen, a partner at Deloitte in Tax Management Consulting, who expressed skepticism about the implementation of Pillar One given their experience in tax consulting.

Nevertheless, Indonesia still maintains its belief in the implementation of Pillar One. This was stated by informant three, where many actions have been taken by the government, particularly the Directorate General of Taxes (DJP) and the Fiscal Policy Agency (BKF), to prepare for Pillar One in Indonesia. The leaders have expressed a high commitment to the potential of Pillar One for national tax revenue. Therefore, in relation to Pillar One, the leaders at DJP and BKF continue to focus on preparing everything with reference to the progress report published by the OECD. Although the substance of Pillar One may not be highly advantageous for the Indonesian government.

### **The Potential Tax Revenue from the Implementation of Pillar One**

One of the provisions of Pillar One, namely Amount A, regulates the allocation of profits provided by the home country of (MNEs) to the jurisdiction or market country where



the MNEs generate profits or earnings. Informant two stated that in simple terms, Pillar One Amount A has the concept of giving and receiving. The home country of the MNE provides benefits in the form of residual profits obtained by the MNE to the market country. The allocation of profits that arises and is received by the market country will generate potential new tax revenue. This is also related to the type of business processes of MNEs, which are shifting towards online business systems. The implication is the blurring of the concept of physical presence (PE) because MNEs engaged in digital business do not need to establish PE to obtain profits. Therefore, market countries or market jurisdictions will not have the right to tax the profits earned by these MNEs, so Pillar One is very good and appropriate for capturing the profits earned by MNEs so that they are not entirely taxed in the home country. Furthermore, with the right to tax the income of MNEs received in the market country, it will realize the principle of taxation on cross-border economic activities (Arnold, 2016 as cited in Surono & Apriliasari, 2022).

OECD (2020b) explains that there are two types of business models included in the scope of Pillar One, namely Automated Digital Services (ADS) and Consumer Facing Business (CFB). In Indonesia itself, according to Surono & Apriliasari (2022), there are 110 MNEs covered by Pillar One. Looking at the data on the Top-100 digital companies and the Top-100 companies engaged in consumer-facing business released by Forbes (2023), there are several companies with market share in Indonesia. Specifically, digital companies tend to PE, while consumer-facing companies may already have PE.

Pillar One Amount A also requires threshold provisions, namely global revenue threshold and de minimis threshold. Companies covered by Pillar One are multinational enterprises with global turnover above EUR 20 billion and profitability (profit before tax to gross income ratio). In addition to being taxed in their home country, these multinational corporations may also be taxed in market jurisdictions if their turnover in the market jurisdiction exceeds EUR 1 million. However, if the Gross Domestic Product (GDP) of the market jurisdiction is less than EUR 40 billion, the turnover threshold in the market jurisdiction is only EUR 250,000. Then, once both threshold tests are met, the tax received by the market jurisdiction is calculated based on the allocation of profits formula.

The provisions in Pillar One regulate that market jurisdictions receive taxation rights over residual profits in proportion to their gross revenues. The procedure for calculating the allocation of profits from these residual profits is as follows:

$$\begin{aligned}\text{Global Residual Profit} &= \text{Profit Before Tax} - (\text{Global Revenue} \times \text{Profitability Threshold } 10\%) \\ \text{Allocation Percentage} &= \text{Allocation Percentage } 25\% \times \text{Residual Profit} \\ \text{Profit Allocation} &= \text{Allocation Percentage} \times (\text{Revenue from Market Jurisdiction} / \text{Global Revenue})\end{aligned}$$

In a simpler formula, the calculation of profit allocation to the market jurisdiction is as follows:

$$\text{Market Profit Allocation} = (\text{Revenue from Market Jurisdiction} / \text{Global Revenue}) \times 25\% \times (\text{Profit Before Tax (Global)} - (10\% \times \text{Global Revenue}))$$

Surono & Apriliasari (2022) in their research, conducted a simulation to calculate the potential tax revenue obtained based on Amount A using Alphabet Inc as a sample company, which is the parent company of Google. The assumption used was EUR 1 = Rp15,000, using revenue data released by Alphabet Inc. The results showed that with a global income of EUR 253,053,000,000, Indonesia could obtain additional tax revenue of Rp53,598,847,500 or 0.01%. This is a relatively low value considering Indonesia's status as a large market or target market for Google.



The discussion of the additional tax revenue potential is supported by statements from informant one, informant three, and informant four, who argue that the allocation of profits received by market countries including Indonesia is considered small. Looking through several studies, it is indeed stated that developing countries will benefit from the implementation of Pillar One Amount A but with a small value. According to Jacobs (2022) with Pillar One, a jurisdiction will receive revenue of 0.026% of GDP. Calculations yielding similar results have actually been conducted by the OECD through Economic Impact Assessments, which was published in 2023. OECD (2020) states that the additional revenue globally is less than 1% of total global corporate income tax.

Furthermore, by categorizing countries into 2 (two) types based on income and corporate tax rates, it is found that high, middle, and low-income countries receive small additional revenue. However, countries which classified as low-income countries receive more additional revenue compared to the other 2 categories. When it is viewed from the group based on income tax rates, the group with rates below >10% and between 10% to 20% will experience losses due to revenue loss. The additional tax revenue potential from Pillar One for Indonesia is also explained by Barake & Pouhaër (2023). Using Forbis 2000 data adjusted with data from the NACE Rev.2 core code to exclude companies whose primary business types are outside the scope of Pillar One, data on 69 MNE groups within the scope of Pillar One, including a threshold of 20 billion euros and profitability of 10% was obtained. The results of the study show that the tax revenue potential received by Indonesia is quite low, at 0.1%. Starkov & Jin (2022) also specifically states the potential revenue obtained from Pillar One by Indonesia. The calculation basis uses FactSet data, categorizing MNEs based on profit before tax and sales according to the Pillar One Amount A threshold of EUR 20 billion and EUR 10 billion. The research results indicate that the amount of potential tax revenue received by Indonesia is USD306 million (EUR 10 billion threshold) and USD247 million (EUR 20 billion threshold).

The low potential tax revenue that countries will obtain due to the implementation of Pillar One can be attributed to schemes such as relief mechanisms regulated within Pillar One, such as the marketing and distribution profit safe harbor (MDSH) and elimination of double taxation. Providing profit allocation based on Pillar A provisions leads to a system of double taxation. Profits allocated will be taxed, as well as the income received by MNEs provided that they have subsidiaries in Indonesia that have also been taxed. Therefore, a scheme is needed to eliminate concurrent taxation on the profits earned by MNEs.

The discussion regarding the potential additional tax revenue received by Indonesia requires careful consideration and precise calculation. Moreover, Indonesia has become one of the countries committed to implementing Pillar One and has agreed to the entire discussion process as outlined in the July Statement, including the dynamics that will emerge later on. In relation to this, informant three stated that it is too early to determine the value of potential additional tax revenue. The discussion of the potential Amount A of Pillar One in the future will bring some differences between the calculations previously done by both the OECD and experts and the actual values after Pillar One is implemented.

#### **Policy Adjustment for the Implementation of Pillar One**

Pillar One including the provision of Amount A is categorized as a multilateral agreement (Multilateral Convention) that, according to the OECD, it requires global approval or consensus to be implemented in a country. OECD (2023) states that after the member countries of the inclusive framework approve the concept of Pillar One MLC, ratification must be carried out. This ratification process may take a long time. According to informant one, in Indonesia, the ratification process takes 2 (two) years. Not to mention the process of adjusting the substance of Pillar One implementation into domestic law.



The plan for implementing Pillar One in Indonesia will be stipulated in a Regulation of The Minister of Finance. Informant three explains that currently in Indonesia, there are existing regulations that becomes the key to the implementation of Pillar One, outlined in Law Number 7 of 2021 concerning Tax Regulation Harmonization (Tax Harmonization Law) and Government Regulation Number 55 of 2022 concerning Adjustment of Tax Regulations. Article 32A of the Tax Harmonization Law states that:

*“In order to enhance economic relations, particularly in the field of taxation, with partner countries or jurisdictions and in line with the dynamic landscape of international taxation, the Government of Indonesia is empowered to establish and/or implement agreements and/or arrangements with the government of partner countries or jurisdictions, both bilaterally and multilaterally, through applicable specialized legal instruments (lex specialis) for the purpose of avoiding double taxation and preventing tax evasion, preventing tax base erosion and profit shifting, exchanging tax information, providing tax collection assistance, and other forms of tax cooperation”*

The provision in the Tax Harmonization Law was further refined through Government Regulation Number 55 of 2022 by adding the term "digitalization of the economy," and the authority was delegated to the Directorate General of Taxes to collaborate with the authorities of partner countries or jurisdictions. According to informant one and informant two, these provisions serve as the basis for drafting Regulation of Minister of Finance containing provisions from Pillar One. After Pillar One is approved and implemented, the International Tax Directorate will collaborate in the drafting of the regulation with other directorates such as the Directorate of Tax Regulations and the Directorate of Compliance, Potential and Revenue, as well as the Fiscal Policy Agency.

Regarding the implementation of Pillar One into domestic law in various member countries, including Indonesia, OECD (2020) provides four minimum aspects that must be adjusted. Domestic laws must be drafted in line with the content of Pillar One Amount A and grant taxation rights to market countries, including taxpayers, tax objects, as well as provisions regarding tax rates and tax years. Additionally, domestic laws must also regulate the elimination of double taxation and an administrative system that facilitates compliance, supported by clear legal certainty regarding Amount A. Based on the minimum requirements set by the OECD, Indonesia must discuss and draft provisions that thoroughly regulate in detail because including tax supervision and regarding tax treaties. Not to forget that through Pillar One, there is a possibility of changes in the behavior of MNEs as a taxpayer.

Pillar One is initiated based on the need to levy taxes on the activities of MNEs as their business begins to shift in digital form. Therefore, how Pillar One is applied will directly affect MNEs, including potentially triggering new actions from MNEs which has subsidiaries in Indonesia. From a digital business perspective, Indonesia is a profitable market for MNEs and that makes no reason for MNEs to withdraw their subsidiaries from Indonesia. Informant three stated that there is a small possibility of MNEs withdrawing from Indonesia due to market considerations and considering the current formulation, Pillar One Amount A along with the double taxation elimination scheme and MDSH does not significantly disadvantage MNEs. Additionally, informant four also added that the provisions of Pillar One are considered to further facilitate MNE business activities because managerial matters related to profit allocation are only at the Ultimate Parent Entities (UPEs) level.

Nevertheless, there is also the potential for MNEs to exploit Pillar One. Informant one explains that with Pillar One, not all UPEs bear the profit allocation under the Pillar One formulation. Subsidiaries in market jurisdiction can also bear it if they have significant profits. Subsidiaries with significant profits tend to operate in business models such as marketing and research and development (R&D) that produce intangible assets. Meanwhile, those operating in business models such as manufacturing do not have significant profits. This condition may allow an MNE to manipulate by inflating or deflating profits, affecting the profit allocation





included in the Amount A formulation. Such actions by MNEs can be classified as tax avoidance.

Tax avoidance is a natural behavior for taxpayers, including MNEs. Through Pillar One, there is a significant potential for MNEs to engaging in tax avoidance and tax evasion due to the provisions of tax enforcement and specific transfer pricing regulations. OECD (2023) states that tax authorities are expected not to carry out supervisory actions related to taxpayer compliance within the scope of Pillar One Amount A. Supervisory actions in this regard encompass all components included in the calculation of Amount A, including MDSH and elimination of double taxation. In essence, tax authorities cannot conduct supervision activities on supporting components of Pillar One Amount A from MNE taxpayers, especially business profits. This provision is limited to Pillar One Amount A but for other components such as income from outside the business, tax authorities can undertake supervision actions. The implication is that MNEs can shift non-business profits to business profits, leading to intense discussions between MNEs as taxpayers and tax authorities.

Therefore, in formulating policies related to Pillar One, provisions regarding tax avoidance must be included to accommodate the potential tax evasion that arises from the implementation of Pillar One. According to informant five, in the policy-making process, the government should strengthen the General Anti Avoidance Rule (GAAR). In addition to aiming to strengthen regulations regarding tax avoidance, strengthening GAAR is also a form of anticipation because transfer pricing for MNEs is also simplified under Pillar One.

Another opinion expressed by informant four is that existing and binding tax regulations of Multinational Enterprise (MNE) should be refined, meaning that existing regulations should be changed as minimally as possible. Additionally, tax regulations exempting MNEs from the entirety of Pillar One are also necessary. However, according to informant four, implementing these suggestions would be very difficult considering Indonesia's full commitment to the implementation plan of Pillar One. Moreover, Pillar One will establish a Multilateral Convention (MLC) that holds legal status above domestic law and even tax treaties.

The existence of the Multilateral Convention (MLC) related to Pillar One will also impact the adjustment of provisions in tax treaties or Double Taxation Avoidance Agreements (DTAs). OECD (2020) elaborates that the presence of the MLC will automatically adjust the provisions in DTAs without the need for bilateral negotiations or discussions between partner countries. This aligns with the opinion of informant three, which states that the position of the MLC is above Tax Treaties and domestic tax law. Matters related to provisions, including formulation and disputes under Pillar One, will refer to the MLC. Meanwhile, matters outside of Pillar One that impact tax treaties will still refer to the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI).

Adjustments to tax treaties through the MLC will be made regarding disputes arising between countries over the implementation of Pillar One. If a dispute occurs, it will be resolved according to the provisions set forth in the Pillar One MLC because Pillar One-related disputes cannot be resolved bilaterally and must be settled through arbitration. Furthermore, according to informant three, the process of arbitration is not recognized in tax treaties. Pillar One also encourages the resolution of disputes using the mutual agreement procedure (MAP).

#### **Adjustments to the Taxation System for the Implementation of Pillar One**

Adjusting policies or domestic laws in Indonesia regarding Pillar One will change the taxation system in terms of administration, system infrastructure, also technology and human resources. From an administrative perspective, OECD (2023) states that the administrative system in domestic law related to Pillar One must be established with a good system to avoid disputes in its implementation. Good administration starts from the initial stage, which is reporting stage.





Pillar One Amount A will be implemented with a self-assessment concept and using a document package scheme. According to informant four, this will be similar to the reporting that is currently in place, including in Indonesia, such as the Country-by-Country Report (CbCR). According to OECD (2023), all jurisdictions will use an XML scheme that supports electronic filing and even data exchange for all information related to Pillar One Amount A. OECD (2023) also adds that the use of standardized self-assessment and document packages aims to provide advantages for MNEs in terms of:

- a. Reducing the burden on multinational enterprises group because each subsidiary can provide the same documents.
- b. Increasing consistency in the implementation of Amount A because reporting requires specific information and calculations from each entity.
- c. Facilitating tax authorities in reviewing profit allocations for Amount A.
- d. Facilitating data and information exchange and multilateral approaches because each tax authority in every jurisdiction uses the same information.
- e. MNEs will receive guidance in the Amount A reporting scheme.

Through this scheme, MNEs will electronically report their own information and calculations for Amount A to the country where the UPE of the MNEs is located, known as the lead tax administration. This tax authority then validates the documents for components that are missing or not in accordance and confirms with the MNE. Subsequently, the lead tax administration will exchange data with tax authorities in other countries where the subsidiaries of the MNEs are located.

The similarity with the CbCR reporting process and the document package scheme will facilitate Indonesia. Indonesia does not need to perform any administration and will only utilize data and information validated by the lead tax administration. This is because, according to informant one, there is currently no UPE for MNEs within the scope of Pillar One in Indonesia, so it is not possible to become the lead tax administration. However, the question arises whether a separate reporting form by MNEs to the tax authority, the Directorate General of Taxes (DGT), is still necessary considering that Pillar One involves foreign taxpayers. Currently, reporting by foreign taxpayers on Value Added Tax on Trading Through Electronic Systems (PMSE VAT) is regulated under Regulation of Minister of Finance Number 48 of 2020, which was refined through Regulation of Minister of Finance Number 60 of 2022 concerning Procedures for Appointing Collectors, Collection, Deposits, and Reporting of Value Added Tax on the Utilization of Taxable Goods and/or Taxable Services from Outside the Customs Area into the Customs Area through Trade Using Electronic Systems.

The Amount A reporting scheme will address the weaknesses of the CbCR system, as highlighted by Surono & Apriliasari (2022), who stated that CbCR cannot identify MNEs if they do not have a permanent establishment in Indonesia because Taxpayer Identification Number (TIN) is required. Additionally, considering that most MNEs in scope of Pillar One operate primarily in the digital business model and do not require a permanent establishment to conduct business activities. Through the Amount A reporting scheme, Indonesia will obtain information about MNEs engaging in sales and generating profits without requiring single identification from the DGT.

Implementing this reporting scheme will also pose challenges for Indonesia in terms of developing information and technology systems. DGT can either develop new systems or leverage updates to the core tax administration system. Informant three states that the Pillar One-related system will be aligned with the development of core tax. One of the core tax business processes that can be related to informant three's statement is the data management process. DGT (2021), through the Core Tax Reform Newsletter, stated that the data



management business process includes Exchange of Information (EOI), Third Party Data Processing, and Data Quality Management.

The development of information and technology systems is not solely undertaken when Pillar One has been implemented. During the process leading up to the implementation of Pillar One, the DGT must also continue to develop systems to support taxpayer business processes, as articulated by informant five. The taxpayer business model in this case, particularly for MNEs, is increasingly moving towards digitalization without a corresponding increase in tax revenue. It requires more efforts from tax authorities to continually update information systems. This is aimed at ensuring that tax authorities can operate in alignment and not lag behind taxpayer business processes. Moreover, considering that Pillar One is planned to be implemented in 2025 or later, DJP can continue to develop systems until Pillar One is fully implemented.

In addition to administration and IT systems, another aspect that can be affected by Pillar One is human resources. It requires resources that truly understand and are competent in Pillar One-related matters. Informant one states that capacity building is needed for individuals who will be involved in Pillar One Amount A provisions with the hope of enhancing individual capacities and capabilities. Moreover, Pillar One which will be adopted into a Regulation of Minister of Finance, will certainly be communicated to all units within the DGT, thus requiring a policy socialization process. This is especially crucial for units overseeing MNEs as taxpayers, such as the Large Tax Office II. Informant four explains that unit is likely to be significantly affected. The impact will be felt in terms of slightly reduced workload since there will be no validation from the beginning for MNEs falling under Pillar One. However, competent employees, especially Account Representatives and Tax Auditor are still required. Furthermore, informant four also adds that an increase in the number of employees is needed in units responsible for Pillar One, such as the Directorate of International Taxation, even though this directorate currently has a working group, namely the Task Force of Digital Economy (TFDE).

### **Alternative Policies Apart from Pillar One**

The implementation of Pillar One, which is still in discussion and shows potential for even longer delays or potentially cannot be implemented at all, has led member countries of the inclusive framework and OECD/G20 to consider seeking alternative measures. The goal is to ensure that the potential tax revenues from digital transactions can be collected by the countries where MNEs are located. One possible alternative is the implementation of Digital Service Tax (DST), which is a form of unilateral measure. Asen & Bunn (Asen & Bunn, 2021)(2021) state that many European countries have already implemented DST, such as Austria, Belgium, Portugal, Turkey, the Czech Republic, France, Hungary, Italy, Poland, Spain, and the United Kingdom. The most recent implementation of DST was carried out by Canada starting on January 1, 2024, as stipulated in the Digital Service Tax Act. Canada imposes a 3% tariff on certain income from online marketplace services, online advertising services, social media services, and the sale or licensing of user data. This DST will apply to all businesses, both domestic ones with a threshold of CAD 20 million and foreign ones with a threshold of EUR 750 million.

According to informant one, DST benefits countries because it is imposed on total revenue or turnover, even though the rate is only around less than 10%. Compared to Amount A, this value is significant considering that the tax from Amount A is based on only 25% of residual profit. Additionally, through DST, tax authorities in a country can make both domestic and foreign companies subject to taxation provided they meet the specified threshold. DST is a potential measure that may also be implemented in Indonesia.



Currently, Indonesia is not able to implement DST. The first reason is the lack of legislation to serve as the basis for implementing DST. The law governing DST or Electronic Transaction Tax (ETT) during the COVID-19 pandemic was regulated by Government Regulation in Lieu of Law Number 1 of 2020, which was amended into Law Number 2 of 2020 concerning State Financial Policies and Financial System Stability for Handling the Corona Virus Disease 2019 (Covid-19) Pandemic and/or In Order to Confront Threats Endangering the National Economy and/or Financial System Stability. In this regulation, the government included articles that provided the basis for Indonesia to impose taxes on electronic transactions. However, this regulation could not be applied again because it underwent a judicial review due to the end of the COVID-19 pandemic status and was revoked by the government. Therefore, the government lacks the legislation and needs to draft new laws. Furthermore, according to informant one, DST cannot be directly categorized as Income Tax.

The second reason is that Indonesia has fully committed to Pillar One Amount A. The consequence as stated in the July Statement, is that countries cannot implement DST or similar measures until the end of 2024 or until Pillar One is implemented in 2025. In relation to this, Indonesia will face difficulties in implementing DST. Moreover, according to Goulder (2023), there will be opposition from the United States, which views DST as discriminatory. The same sentiment was expressed by informant four, stating that any policy adopted by Indonesia, including DST, would be vulnerable to challenges from the United States. The International Chamber of Commerce (ICC) has also sent a letter to the OECD requesting an extension of the period without the implementation of DST (Goulder, 2023).

Nevertheless, according to Informant six, every country must still prepare and design regulations related to DST. The mindset should be at least similar to what Canada and European countries are considering or have implemented regarding DST. Pillar One will not progress anywhere even though discussions on the implementation of its provisions are ongoing. Like Canada, countries should not compromise on waiting longer for the implementation of Pillar One, considering that the longer Pillar One is delayed, the more potential revenue countries will lose. Moreover, the development of digital technology will continue to be massive and the influence of the United States which is currently considered very strong, will persist.

The potential implementation of DST in Indonesia, according to Informant six, could be realized in the future. This statement is based on the potential economic development of Indonesia, which will have an increasing influence in the future. MNEs will inevitably direct markets to countries with the potential for significant income generation. This is where Indonesia gains power or influence to strengthen its position concerning the United States, including cooperation in international taxation especially the implementation of DST. Therefore, it all boils down to the bargaining power of a country particularly because, according to Informant six, the size of the economy will attract investment. Another alternative related to DST might also replicate the method adopted by European countries. According to Informant three, European countries that have implemented DST made a deal agreement with the United States, wherein the agreement included a credit method for DST collected from multinational companies originating from the United States. More precisely, in planning to use DST as an alternative to Pillar One, Indonesia must be able to make the right political approach to the United States.

Another alternative that Indonesia could implement to replace Pillar One is the adoption of Article 12B of the UN Model Tax Convention. According to Informant six, this model is perceived as simpler and easier to implement compared to Pillar One. Article 12B does not use profit allocation formulas and is solely based on the income received by MNEs, specifically directed towards Automated Digital Services. The country where the MNE is located

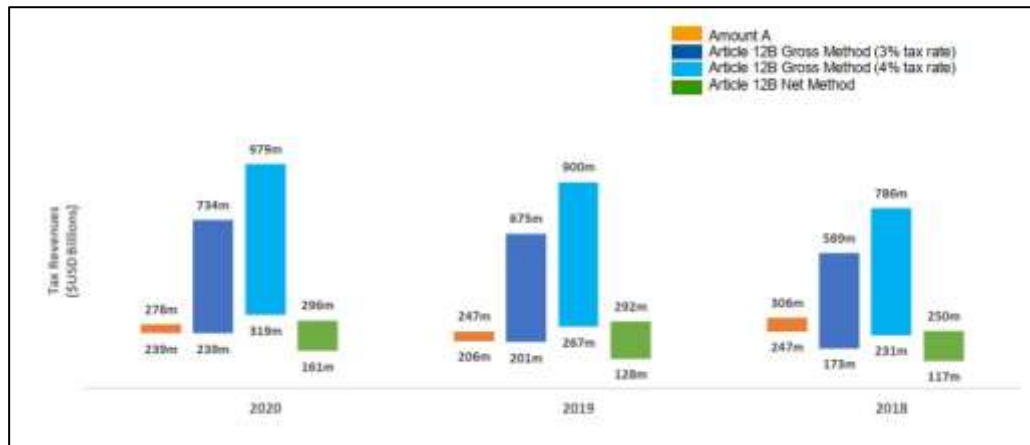


automatically has the right to tax the income generated. Article 12B does not require a de minimis threshold, so all forms of businesses can fall under its scope.

In Article 12B, it regulates the categories of Automated Digital Services (ADS) that fall within the scope of this article. According to PWC (2021), these categories include: (i) *online advertising services*; (ii) *supply of user data*; (iii) *online search engines*; (iv) *online intermediation platform services*; (v) *social media platforms*; (vi) *digital content services*; (vii) *online gaming*; (viii) *cloud computing services*; and (ix) *standardised online teaching services*. All forms of services related to the natural business processes of ADS can also be subject to taxation, including professional services, internet network provision services, online teaching services, sales of goods and services other than ADS, and income from the sale of physical goods regardless of network connectivity. These categories can help demonstrate the existence of MNE activities that generate income from the source country. Informant six states that with Article 12B, all forms of business activity representation, including individuals, as long as they generate income, will be subject to taxation on that income.

According to Starkov & Jin (2022), Indonesia can benefit greatly from the implementation of Article 12B.

Figure 1. The comparison of tax revenue potential between Amount A and Article 12B



Source: Starkov & Jin (2022)

If we look at Figure 1, it appears that the potential tax revenue from Article 12B is larger compared to Amount A. This difference is based on the tax base of each provision. Amount A uses a profit allocation of 25% from residual profit, whereas Article 12B employs two methods: the gross method and the net method. The gross method is based on the total revenue of the MNE, which can be considered as turnover, while the net method is based on profit. Therefore, Starkov & Jin (2022) state that for Indonesia, Article 12B is more favorable than Amount A.

An aspect that may be of concern regarding Article 12B is that this provision requires changes or adjustments to tax treaties. Indonesia, as the country where income is sourced and will implement this provision, must negotiate with the home countries of the MNEs. The same will happen if a country implements unilateral measures like DST. Therefore, Article 12B cannot yet be implemented, considering that as discussed earlier, the majority of MNEs originate from the United States and for now, similar measures to DST are not accepted by the United States. This potential hindrance in the negotiation process for adjusting tax treaties.

One potential alternative currently being explored as a method of taxing digital transactions is through value-added tax (VAT) or withholding tax. Informant six asserts that maximizing the collection of similar VAT or withholding tax at the time of transactions or using a point-of-transaction approach is feasible. Indonesia has implemented PMSE VAT, but it still does not fully accommodate income received by entities engaged in digital business activities.



Meanwhile, regulations regarding taxation of digital transactions are already stipulated in Article 32A of the Income Tax Law, which states that the Minister of Finance can appoint collectors for electronic-based transactions. However, according to informant one, this cannot be used as a reference because there are no specific provisions regarding taxation of electronic transactions in Indonesia. Additionally, imposing withholding tax may conflict with the home countries of MNEs, such as the United States.

The addition of criteria for Permanent Establishment (PE) is also considered as an alternative to collect tax revenue from digital transactions. Informant four emphasizes that the criteria for PE that need to be added in domestic regulations and tax treaties include the concept of "significant economic presence." This is an update to the definition of PE, as the traditional concept of physical presence is no longer relevant due to the evolving nature of digital business models. Significant economic presence means that when an entity conducts significant economic activities, including generating income in a country, the source country can levy taxes on that entity. When associated with MNEs operating digital business models in Indonesia, this concept is highly relevant, as digital MNEs clearly earn income from Indonesia. Informant five adds that this concept also needs to be included in tax treaties. However, according to informant six, the concept of significant economic presence is more complex than the economic presence criteria outlined in Article 12B of the UN Model Convention. Additionally, adding these alternative criteria for PE would also intersect with the interests of the United States as the home country of the largest number of major MNEs. Therefore, it seems like a similar cycle is created with each alternative to Pillar One.

## **CONCLUSION**

### **Conclusion**

Currently, Pillar One cannot be implemented in Indonesia because a global agreement has not been reached yet. This is due to constraints experienced in the negotiation process, primarily involving the United States. The United States, as the country with the largest number of MNEs in the scope of Pillar One, feels that it is unfair and that Pillar One tends to be discriminatory because it requires the United States to share tax revenue with market countries. Additionally, the provision for OECD/G20 Inclusive Framework on BEPS member countries not to implement digital transaction taxes until Pillar One is signed and agreed upon has led to countries like Canada not fully committing to Pillar One. However, Indonesia also plays a role in shaping the discussions on Pillar One due to its position and influence.

Pillar One will have an impact on Indonesia's tax revenue because Indonesia is likely to receive profit allocations according to the Amount A formula of Pillar One. However, the potential tax revenue obtained from profit allocation tends to be low due to the existence of relief schemes such as marketing and distribution safe harbor and elimination of double taxation. There is also a possibility that Indonesia will not receive additional revenue from the Pillar One Amount A. This is supported by research showing similar results, namely, low revenue potential for developing countries, of which Indonesia is one these countries.

When Pillar One enters the in-force period according to the July Statement of the OECD/G20, Indonesia must be able to adapt Pillar One into domestic law in accordance with OECD guidelines. The government particularly the Directorate of International Taxation and the Fiscal Policy Agency, plans to draft the adoption of Pillar One into a Regulation of Minister of Finance. Policy adjustments must also consider the conditions or impacts that Pillar One will have on the behavior of MNEs as subjects.

The tax system consists of reporting administration, information systems, and human resources. Pillar One reporting is planned to resemble Country-by-Country Reporting (CbCR) with a self-assessment system and document packages. This system will significantly facilitate





both MNEs and tax authorities in reporting administration because of a single data source and validation performed only by the tax authorities at the MNE's headquarters. The reporting mechanism of Pillar One will then lead to the demand for the development of information technology (IT) systems. Updates to the Core Tax will be synchronized with the reporting system of Pillar One. Additionally, the IT system is expected to be further developed to align with the evolving business models of taxpayers, particularly towards digital business models. Pillar One will also affect the readiness of human resources, especially in terms of technical competence and expertise, as well as the addition of competent staff related to Pillar One. Therefore, if Pillar One is implemented, there will be many activities aimed at enhancing the competence of human resources, such as capacity building and socialization.

There are three alternatives that the DGT can choose if Pillar One is not implemented or is canceled. The first alternative is the implementation of Digital Service Tax (DST). DST has been implemented and is operational in several countries, primarily in Europe. Canada also plans to implement DST in 2024. DST is considered an alternative because, in addition to global MNEs, tax authorities can also collect taxes from local companies with digital business models. Indonesia currently cannot implement DST due to a judicial review of the DST provision, which is Law Number 2 of 2020. Additionally, Indonesia which has fully committed to the Pillar One negotiation process, is prohibited from implementing DST or similar taxes. However, Indonesia still has the potential to implement DST considering the large market potential in Indonesia in the future.

The second alternative is the application of taxing rights to MNEs operating Automated Digital Services (ADS) with a scheme outlined in Article 12B of the UN Model. Compared to Pillar One, this alternative is more advantageous in terms of generating substantial tax revenue. This is because the tax base, or the value subject to taxation, is derived from turnover (gross method) and profit (net method). Furthermore, Article 12B of the UN Model is simpler in terms of the presence of MNEs in a source country because presence can be determined by the smallest activities of an MNE in efforts to generate income.

Another alternative is the addition of a significant economic presence criterion as part of the Permanent Establishment (PE) concept. Adding this criterion serves as a solution to the increasingly prevalent digital business models. These alternatives to Pillar One can be implemented by Indonesia, although all alternatives require modifications to tax treaties. Additionally, Indonesia still needs to engage with countries where MNEs are headquartered, including the United States, which may pose challenges.

#### **Saran**

Pillar One, developed by OECD/G20 Inclusive Framework on BEPS member countries, currently cannot be globally implemented, including in Indonesia due to various constraints. Information gathered also indicates limited optimism and a belief that Pillar One may not be feasible. A suggestion that researchers can offer to the government, particularly the Directorate General of Taxes, is to reevaluate the cost and benefits and commitment to the implementation plan of Pillar One. The cost and benefits should be assessed based on the implications that may arise from the implementation of Pillar One, especially concerning the potentially low tax revenue.

There are many alternatives and options besides Pillar One to capture and accommodate tax revenue from digital transactions. Alternatives such as Digital Service Tax, Article 12B of the UN Model, and the addition of the significant economic presence criterion in the PE concept can be viable options because they allow Indonesia to potentially gain significant additional tax revenue compared to the potential tax revenue from Pillar One. However, these alternatives may not be chosen by the government considering the global conditions and dynamics heavily



influenced by major economies like the United States. Nevertheless, it's not impossible for these alternatives to be pursued with the right political approach towards these major countries.

In addition to alternatives to replace Pillar One policy, the DGT can also leverage the development of tax administration systems towards the digital economy. The Business to be aspect of PSIAP is expected to capture the potential revenue from digital transactions. The reason is that the implementation of Pillar One continues to be delayed until 2025, and it is possible that it will be further delayed, and alternative policies to Pillar One are also not possible to be applied. Therefore, to fill the gap in efforts to increase state revenue from the digital economy sector, the option that DGT can take is from the perspective of developing tax administration systems. Although it does not directly increase revenue potential, with system development, DGT can align with the development of the digital economy with the hope of at least balancing the processes of taxpayers' businesses.

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